COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS
AND ENERGY

Investigation by the Department	**)**	
of Public Utilities Upon its Own	**)**	
Motion Commencing a Rulemaking	**)**	
Pursuant to 220 C.M.R. §§ 12.00 et seq.,	**)**	**D.T.E. 97-96**
Revising Standards of Conduct	**)**	
Governing the Relationship Between	**)**	
Local Distribution Companies and Their	**)**	
Affiliates	**)**	

REPLY COMMENTS
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THE BERKSHIRE GAS COMPANY

INTRODUCTION

The Company notes that other comments filed provide considerable support for and agreement with the positions taken by the Company in its Initial Comments in this proceeding. The utility company comments strongly stress the efficiencies and cost savings to utility ratepayers that result from the sharing resources with an affiliate or non-utility division. In addition to this practical reason for not expanding the Standards, Dr. Kahn and Dr. Morey clearly expounded on the economic policy reason for not expanding the Standards, i.e., that efficiency should not be hindered and that competition , not competitors, should be protected. Even the consumer and competitor parties do not dispute that such savings occur. These parties' arguments (other than arguing against perceived favoritism to affiliates) rely on the reasonableness of cost allocations. That concern, however, can be addressed fairly, without imposing undue restrictions on utility corporate structure and relationships.

Likewise, the Company's other main point, is also in agreement with many other comments, i.e., that existing means of protecting ratepayers through reporting and cost allocation requirements make unnecessary an expansion of the Standards . By means of full and thorough cost allocations to non-utility activities, ratepayers will be fully compensated for the resources used by the non-utility affiliate. In fact, it is likely that the utility ratepayers will benefit from such sharing of resources. See, e.g., Tr. 62-63.

As discussed in greater detail below, the comments of the non-utility entities state support for the desirable goals of protecting competition and protecting utility ratepayers from cross-subsidization of non-utility efforts. In some cases it is clear that those commenters actually want to handicap the utility affiliate and thereby lessen competition to the services they provide. In other cases, the comments simply go too far in seeking ratepayer protections and would result in burdens upon non-utility affiliates and reduced benefits to utility ratepayers. Further, the Company again stresses that Standards which may be justified for utility affiliates in the energy markets are not necessary or proper for non-energy markets. That the Federal Energy Regulatory Commission does not apply its Standards of Conduct to non-energy affiliates of pipeline companies supports this view. See FERC Order 497- E.

These reply comments address both certain points raised by the initial comments or in the December 8, 1997 hearing and certain questions raised by the Department staff during the hearing. Specifically, the Company discusses: (1) the best approach to avoiding improper cross-subsidization both as to allocation of shared costs and compensation for transferred assets, (2) implications of the new electric restructuring legislation, and (3) the proper accounting treatment of a utility company name and good will.

DISCUSSION

1. Existing Procedures Can Provide Sufficient Protection Against Improper Cross-Subsidization

Neither involvement by utility companies in non-utility (i.e., non-energy) businesses nor associated concerns about cross-subsidization are new issues. While such issues are certainly receiving significant attention currently, the Department has long made significant efforts to avoid cross-subsidization and to ensure that utility/affiliate transactions yielded the fair value for the utility ratepayers. See e.g., Berkshire Gas Company, D.P.U. 92-210, p. 4 et seq. (1993). Generally, this has been accomplished through rate setting proceedings and through proceedings reviewing utility investments. The Company believes that this approach has achieved the goal of preventing cross-subsidization. No comments on this proceeding seem to challenge that conclusion.

The Attorney General suggests that there should be a specific proceeding initiated to consider proper cost allocation methods. The Company suggests rather that the applicability of a given allocation methodology depends on the special factual circumstances of a specific utility, so that such a special proceeding would not be productive.

DOER suggests that rate cases are too infrequent now to assure proper cost allocation, but that concern is misplaced. Though rate cases may be less frequent, where a case establishes cost allocations, those allocations will be accurate for some time following the rate order. Also, performance based regulation through price caps is likely to become more prevalent. That means that proper allocations will be made as of the "cast off" time and after that the non-utility operation is essentially a risk of the utility. As to the transfer of utility rate base assets to an affiliate, in the past the Department has ensured that the ratesetting process captures the requisite value for ratepayers, even where the transactions occurred at a time several years before the test year.[1] This same approach, in a PBR context or not, will ensure ratepayer protection.

The additional protection proposed by Boston Gas of the utility filing notice of affiliate transactions seems to be already encompassed by the ratemaking process (or perhaps also covered by the section 17A process). The Company, however, believes that such a requirement could be positive if limited to transactions over a certain magnitude. That threshold level for

[1]See, e.g., Commonwealth Electric Company, D.P.U. 90-331 (1991).

reporting would most properly be established on a percentage of assets basis in consideration of the varying size of utility companies.

The requirement of a bidding process to maximize value of utility assets transferred to an affiliate, suggested by Bay State, is not unreasonable for certain assets, e.g., bulk sales contracts in an emerging competitive market.[2] However, if applied to broadly, such a requirement could be unduly cumbersome and even violate some market efficiencies as suggested by Dr. Kahn (i.e., advantages due to corporate positioning are not, per se, anti-competitive. Tr. 61).

2. Implications Of The New Electric Restructuring Legislation

Both utility and other commenters have relied upon the new Electric Restructuring legislation (the "Act") to support their views that the Standards should either remain unchanged or be expanded. One point that has not been mentioned is that the Act specifically does apply in certain cases to gas utility companies (e.g., Act sections 119, 307, 315), but with respect to the standards section (Act SECTION 193, adding section 1C to General Laws chapter 164) that clear coverage of gas companies is absent. Therefore, at the least, the Company believes that reference to the Act cannot support expansion of the Standards to gas utility companies. Further, the Company believes that the better reading of the Act is to limit the Standards section applicability to the general subject matter of the Act --- electric competitors.

3. Corporate Affiliates Should Be Able To Use A Corporate Name And Goodwill Without Payment To Ratepayers

In the Initial Comments and the December 8, 1997 hearing, two issues concerning utility corporate names and goodwill arose. First, concerning the use of the name, the Company agrees that the existing restriction on an energy marketing affiliate's use of the utility name is appropriate to avoid customer confusion and to assist the development of competition in the energy marketplace. Green Mountain Energy is correct, however, that the goal of customer knowledge also requires that it is proper and necessary for marketers to disclose their

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[2]See Global Petroleum, D.P.U. 96-66 (1997).

ownership. In the non-energy commodity markets the advantage of the incumbent utility is not such a potential problem, however, so any restrictions on use of a corporate name should not be extended.

Second, there should be no requirement of compensation for use of the corporate name. Though there is precedent from other states on both sides of the issue.[3] The Company believes there are two compelling reasons why no compensation is due to ratepayers for the use of a utility corporate name. First, as observed by the Bay State witness (Tr. 216), utility rate setting has never encompassed a component, either as a cost or an asset, reflecting a value for a corporate name or goodwill. In fact, the Department has explicitly excluded from allowable expenses in the ratesetting process, the costs of institutional, or image, advertising and corporate identification, both of which are the only costs factored into rates that specifically relate to development of the value of a corporate name. Boston Gas Company, D.P.U. 96-60, p. 63 (1996); Berkshire Gas Company, D.P.U. 92-210, p. 99 et seq. (1993); Commonwealth Electric Company, D.P.U. 956 p. 31 (1982). Therefore, in Massachusetts it is shareholders who have paid for developing value in a corporate name, so no compensation should be due to ratepayers.

In response to the argument that ratepayer payment for utility services created the value in the name, the Company believes that the perspective of the Minnesota Supreme Court is compelling:

> Certainly, ratepayers are involved in building a gas utility's good will when they purchase utility service. However, ratepayers are no different in that regard than any consumer who purchases a product from a business. The simple act of purchasing a product or service from a business does not mean that the consumer becomes an owner of any of the business' assets. n5 Nor does it mean that the

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[3] Minnegasco v. Minnesota Public Utilities Commission, 549 N.W.2d, 904, 1996 Minn. Lexis 368, 169 PUR 4th 405 (1996). (No compensation due ratepayers for affiliate's use of utility. Name and goodwill); Rochester Telephone Corp. v. New York Public Service Comm'n, 87 N.Y.2d 17, 637 N.Y.S.2d 333, 660 N.E.2d 1112 (1995). (Compensation regained, but such compensation may be through the benefit of cost sharing.)]

consumer bears the cost of creating good will. The relationship between the ratepayer, as a consumer, and the gas utility, as [**12] a business, does not change just because the gas utility provides regulated utility services. The ratepayer remains a consumer and the assets remain the property of the utility.

n5 This is consistent with Justice Marshall's observation in his concurring opinion in Pacific Gas & Electric Company v. Public Utilities Commission of California, 475 U.S. 1, 22 n.1, 89 L.Ed.2d 1, 106 S.Ct. 903 (1986). Justice Marshall said:

[A] consumer who purchases food in a grocery store is paying for the store's rent, heat, electricity, wages, etc., but no one would seriously argue that the consumer thereby acquires a property interest in the store. That the utility passes its overhead to ratepayers at a rate fixed by law rather than the market cannot affect the utility's ownership of its property * * *.

Id. (Marshall, J., concurring).

Also, from a competitive perspective there should not be a significant concerns with utility affiliates using the corporate name of the utility because it is not clear that the name provides them any unfair and improper competitive advantage. As noted by some commenters, the positive value of a company name derives from the company doing a good job, not simply from it having been the incumbent. In fact, it is possible that there may not be a positive value to an affiliate's use of the utility name. Further, much of the competition is hardly unknown to customers generally. For example, GE, Exxon, Enron and others have capitalized upon their corporate names in a variety of corporate ventures and one would be hard pressed to imagine that such entities would not be able to compete on an equal basis on the basis of the corporate name factor. Any advantage associated with the utility's name is significantly lessened when the affiliate is acting

4. Other Issues

At the December 8, 1997 hearing the Department staff raised the question of how to protect utility ratepayers from potential adverse effects of diversification upon the utility cost of capital. The Company suggests that such potential adverse effects can be avoided by means of protections crafted in the context of a proceeding upon a request for approval of an investment in an affiliate. More significantly, however, the Company suggests that if utilities are hindered in conducting non-utility activities and are barred from sharing resources and costs thereof that the lost synergies may have a worse impact on the utility cost of capital. To the extent that utilities are restructured and leave the merchant function there may also be adverse effects on the quality of service.

The issues of joint advertising and "rental" of utility billing envelope space have also arisen in this proceeding. The Company believes that utilities should be able to rent their billing envelope space, especially where they do so on a non-discriminatory fashion. Similarly, utilities should be able to establish trade alliances and obtain the benefits from joint advertising, again where their actions are taken on a non-discriminatory basis.

CONCLUSION

In summary, the Company believes that the Department need not and should not expand the Standards. Ratepayers can be well protected under the existing regulatory framework. the Department should encourage and foster creative efforts to diversify and thereby reduce costs to core customers. Any requirement of separation for a small company could easily cause a loss of such efficiencies.